COMMONWEALTH OF VIRGINIA
DEPARTMENT OF THE TREASURY

GENERAL ACCOUNT INVESTMENT GUIDELINES
Statement of Investment Policies and Goals

Adopted By The Treasury Board
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OVERVIEW

The Commonwealth of Virginia, Department of the Treasury manages the General Account Investment Portfolio. These monies are comprised of funds collected and held for various fund groups including the General Fund of the Commonwealth.

This document sets forth the responsibilities of the Treasury and its investment managers relating to the implementation of the investment policy and asset strategy, and evaluation and review of investment performance and progress toward attaining goals.

State Treasury Policy

It is the policy of the State Treasurer to invest public funds in a manner which will provide the highest investment return with the maximum security while meeting the daily cash flow demands of the entity and conforming to all statutes governing the investment of public funds. Investment shall be made with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.

Treasury Objectives

The primary objectives, in priority order of the State Treasurer's investment activities shall be:

1. **Safety.** Safety of principal is the foremost objective of the investment program. Investments of the State Treasurer shall be undertaken in a manner that seeks to ensure preservation of capital in the overall portfolio.

2. **Liquidity.** The State Treasurer's investment portfolio will remain sufficiently liquid to enable it to meet all operational requirements which might be reasonably anticipated.

3. **Return on investment.** The State Treasurer's investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account its investment risk constraints and the cash flow characteristics of the portfolio.

POLICY GUIDELINES

General Account Structure

In order to meet the primary objectives of the State Treasurer, the General Account will be divided into two major pools: a Primary Liquidity Pool and a Total Return Pool. The Primary Liquidity Pool, which will be internally managed by the Treasury Staff, is to be the major source for disbursement requirements and operational needs of the General Account. Safety of principal and liquidity at the expense of return on investment are the foremost objectives of the portfolio.

The objective of the Total Return Pool, which will be externally managed, is to generate an investment return, over the long-term, higher than the return on assets managed internally (Primary Liquidity Pool). To generate higher investment returns, it is recognized that additional interest rate risk and credit risk, within prudent constraints, must be assumed in the management of the Total Return Pool. To further control these risks, and to provide for sufficient management flexibility, the Total Return Pool may be structured into three sub-portfolios: a Short Duration Portfolio, an Intermediate Duration Portfolio, and an Extended Duration Portfolio. However, in seeking higher investment returns, the portfolio managers of the Total Return Pool will be cognizant of the Treasury objectives of safety of principal and liquidity.

Asset Mix Policy

The Treasury's allocation target for the overall General Account asset mix are:

Primary Liquidity Pool	75%
Total Return Pool	25%

The Treasury's allocation guidelines for the Total Return Pool are:

	Target	Minimum	Maximum
Short Duration Portfolio	20%	15%	40%
Intermediate Duration Portfolio	60%	30%	85%
Extended Duration Portfolio	20%	0%	30%

The intent of the Asset Mix Policy is to increase the overall average maturity of the General Account Investment Portfolio to enhance the returns over the long-term. Deviations from the allocation targets for the General Account, and from the guidelines for the Total Return Pool listed below, may be made by the Treasury Investment Staff, when economic conditions or liquidity needs warrant, or when the Treasury Staff determines that the aggregate deviation does not constitute a material departure from the spirit of the target allocation and the intent of the Treasury Board. The Treasury Investment Staff shall review the target allocations and guidelines at least annually.

Investment Guidelines and Restrictions

Authorized Investments

The State Treasurer is empowered by statute to invest in the following types of securities:

1. Obligations issued or guaranteed by the U.S. Government, an Agency thereof, or U.S. Government sponsored corporation. These securities can be held directly, in the form of repurchase agreements collateralized by such debt securities, and in the form of a registered money market or mutual fund provided that the portfolio of the fund is limited to such evidences of indebtedness.

2. Non-negotiable certificates of deposit and time deposits of Virginia banks and saving institutions federally insured to the maximum extent possible and collateralized under the Virginia Security of Public Deposits Act.

3. Repurchase agreements collateralized by the U.S. Treasury/Agency securities. The collateral on overnight or one day repurchase agreements is required to be at least 100% of the value of the repurchase agreement. Longer term repurchase agreements are required to have collateralization in excess of 100% and be marked to market on a regular basis. However, market fluctuations could result in the value of the collateral increasing or decreasing between the valuation and published closing prices.

4. Bankers acceptances with major U.S. money center banks and domestic offices of international banks.

5. Negotiable certificates of deposit and negotiable bank deposit notes of domestic banks and domestic offices of foreign banks.

6. Commercial paper issued by domestic corporations.

7. Corporate notes and busted convertibles of domestic corporations.

8. Taxable Municipal Securities

9. Asset-backed securities and mortgage-backed securities.

10. Dollar denominated obligations of sovereign governments, and their instrumentalities.

11. Commercial Mortgage-Backed Securities (CMBS), Collateralized Mortgage Obligations (CMOs) and Planned Amortization Classes (PACs).

Credit Quality

The State Treasurer will in all cases place emphasis on securities of high credit quality and marketability. Holdings are subject to the following credit quality limitations at time of purchase. Should a security fail to meet the following credit quality limitations after purchase (i.e., credit downgrades), the external manager shall notify the Treasury Investment Officer or Director and the Investment Consultant in writing within one business day, of each security that fails to meet the credit quality limitations. Such security must then be sold within 60 calendar days, or earlier if so directed by Treasury Investment Staff, unless the manager's reasoning to continue to hold the security is approved in writing by the State Treasurer.

1. Bankers acceptances. Bankers acceptances of domestic banks and domestic offices of international banks must be rated no lower than P-1 by Moody's Investors Service and A-1 by Standard & Poor's.

2. Negotiable certificates of deposit and negotiable bank notes. Negotiable certificates of deposit and negotiable bank notes of domestic banks and domestic offices of foreign banks must be rated at least P-1 by Moody's Investors Service and A-1 by Standard and Poor's for maturities of one year or less. They must be rated at least Aa by Moody's Investors Service and AA by Standard and Poor's for maturities exceeding one year.

3. Commercial paper. Commercial paper notes of domestic corporations must be rated no lower than P-1 by Moody's Investors Service and A-1 by Standard & Poor's.

4. Corporate Notes and Bonds and Busted Convertibles. Securities of domestic corporations must be rated A or better by two nationally recognized rating agencies, one of which must be either Moody's Investors Service or Standard & Poor's. This includes all levels of the 'A' rating. However, each external investment manager may invest up to 10% of their portfolio in any rating level of Baa/BBB rated bonds which, at a minimum, must be rated investment grade by two nationally recognized rating agencies (one of which must be either Moody's Investors Service or Standard & Poor's). In addition, all Baa/BBB rated securities purchased in the portfolio must be considered "investment grade" by Lehman Brothers as related to inclusion in the appropriate Lehman index. Busted convertibles must be liquidated prior to conversion to equity. Also, to avoid holding equity-like securities, busted convertibles must be sold when they reach 105% of their bond value.

5. Taxable Municipal Bonds. Taxable Municipal Bonds issued by states, political subdivisions, and agencies of the fifty United States (including D.C.) and its territories. Municipal bonds must be rated A or better by two nationally recognized rating agencies (one of which must be either Moody's Investors Service or Standard & Poor's).

6. Asset-backed securities. Asset-backed securities must be rated AAA by at least two nationally recognized rating agencies (one of which must be either Moody's Investors Service or Standard & Poor's.)

7. Dollar denominated obligations of sovereign governments. Sovereign debt must be rated Aaa by Moody's Investor Service and AAA by Standard & Poors.

8. Commercial Mortgage-Backed Securities (CMBS), Collateralized Mortgage Obligations (CMOs), and Planned Amortization Classes (PACs) must be rated AAA or better by two nationally recognized rating agencies (one of which must be either Moody's Investors Service or Standard & Poor's.) This also includes all private label mortgage-related securities.

Diversification

The State Treasurer will diversify investments by security type and by issuer and the following shall apply:

1. Each portfolio will be diversified with no more than 5% of the value of the fund invested in the securities of any single issuer. This limitation shall not apply to the U.S. Government, or Agency thereof, or U.S. Government sponsored corporation securities and fully insured and/or collateralized certificates of deposit.

2. The maximum percentage of the Primary Liquidity Pool in each eligible security type is limited as follows:

U.S. Treasury and Agency Securities	100%
Non-Negotiable Certificates of Deposit	5%
Repurchase Agreements and/or Money Market Funds	35%
Bankers Acceptances, Negotiable Certificates of Deposit and/or Negotiable Bank Deposit Notes	40%
Commercial Paper	35%
Corporate Notes (Includes taxable municipal securities).	35%
Obligations of Sovereign Governments, and their instrumentalities	10%

3. The maximum percentage of each portfolio within the Total Return Pool in each eligible security type is limited as follows:

U.S. Treasury and Agency Securities	100%
Non-Negotiable Certificates of Deposit	0%
Repurchase Agreements	0%
Bankers Acceptances	0%
Negotiable Certificates of Deposit and Negotiable Bank Deposit Notes	20%
Commercial Paper	0%
Corporate Bonds/Notes (Includes Busted Convertibles)	65%
Taxable Municipal Securities	20%
Asset-Backed Securities	35%
Combined MBS, CMBS, CMO, PAC	60%
Mortgage-Backed Securities (MBS)	50%
Commercial Mortgage-Backed Securities (CMBS)	10%
Collateralized Mortgage Obligations (CMOs) Other Than PACs	10%
Planned Amortization Classes (PACs)	20%

Obligations of Sovereign Governments, and their instrumentalities	10%
Money Market Funds (excluding transitional cash)	10%

4. All money market assets in the Total Return Pool shall be invested in a high quality short-term investment fund designated by the Treasury Staff and made available by the General Account Master Custodian.

Prohibited Investments or Actions

1. Inverse floaters, IOs, POs, and Z-tranche securities.

2. Futures, options, options on futures, margin buying, leveraging, and commodities. Forward trades are permitted as long as they are procured during normal "when issued" periods for individual markets and as long as cash is reserved or a security will mature to cover the purchase.

3. Any security not strictly authorized above must be approved in advance, in writing, by the Treasury Investment Staff.

Duration Limitations

To the extent necessary, the State Treasurer will attempt to match investments with anticipated cash requirements. Additional funds will be invested at maturities determined to be most beneficial to the portfolio. The following duration limitations shall apply:

1. The maximum duration for any single corporate security may not exceed 15 years and the maximum duration for any single asset-backed security may not exceed five years at the time of purchase. In the event the duration subsequently exceeds these limits, the external manager shall notify the Treasury Investment Officer or Director who shall determine whether the security should be sold. The maximum maturity on any single sovereign government obligation, excluding the U.S., may not exceed five years. The maximum maturity on any negotiable certificate of deposit and negotiable bank deposit note may not exceed five years.

2. The target duration (years) for the Primary Liquidity Pool, the Total Return Pool, and each Total Return Portfolio, are as follows:

	Minimum	**Target**	**Maximum**
Primary Liquidity Pool	0.3	1.0	1.4
Total Return Pool	2.0	3.5	4.3
Short Duration Portfolio	1.4	1.7	2.0
Intermediate Duration Portfolio	2.0	3.5	4.2
Extended Duration Portfolio	2.8	5.5	6.9

3. The above target durations, coupled with the Asset Mix Policy previously described, are designed to establish a target duration of 1.6 years for the overall General Account, within a range of 0.4 years at the minimum to 2.3 years at the maximum.

The Asset Mix Policy and the target duration guidelines shall be reviewed at least annually by the Treasury Investment Staff, and modified as conditions warrant.

For purposes of this section, duration shall be defined as the industry standard modified duration as calculated by Bloomberg. In addition, for purposes of asset-backed securities and mortgage-backed securities, the prepayment assumptions to be used in the modified duration calculation will be the Bloomberg median prepayment assumptions. In the absence of a median prepayment assumption available in Bloomberg, the assumption to be used shall be that which provides the greatest principal protection to the portfolio.

Securities Lending

Securities lending will be performed for the General Account portfolio under an approved agreement and separate Securities Lending Policies and Guidelines. Net lending income will be added to the General Account income.

General Account Benchmarks

Total General Account:	Composite weighted 75% Primary Liquidity Pool benchmark, 25% Total Return Pool benchmark
Primary Liquidity Pool:	Treasury One-year Constant Maturity
Total Return Pool:	Composite weighted 20% Short Duration benchmark, 60% Intermediate Duration benchmark, 20% Extended Duration benchmark
Short Duration Portfolio:	Lehman Brothers 1-3 Year Treasury Index
Intermediate Duration Portfolio:	85% Lehman Brothers Intermediate Government/Credit Index, 15% Lehman MBS Fixed Rate Index.
Extended Duration Portfolio:	Composite weighted 83% Lehman Brothers Aggregate Bond Index, 17% Lehman Brothers Long Government/Credit Index.

All General Account benchmarks will be reviewed annually, and adjusted based upon changes in the General Account Structure and/or changes in objectives of the General Account, Primary Liquidity Pool or Total Return Pool.

STANDARDS OF INVESTMENT PERFORMANCE

Performance results of the Primary Liquidity Pool shall be dollar-weighted. Performance results for the Total Return Pool, and for each Pool component, shall be time-weighted and measured net of investment management fees. Volatility risk shall be measured by the standard deviation of annualized quarterly returns.

STANDARDS OF INVESTMENT PERFORMANCE

	Relative Standard (5 years)
Total General Account	Exceed the General Account benchmark by 11 basis points
	Volatility should not exceed 115% of the General Account benchmark
Primary Liquidity Pool	Exceed the Primary Liquidity Pool benchmark by 10 basis points
	Volatility should not exceed 110% of the Primary Liquidity Pool benchmark
Total Return Pool	Exceed the Total Return Pool benchmark by 46 basis points
	Volatility should not exceed 120% of the Total Return Pool benchmark
Short Duration Portfolio	Exceed the Short Duration Portfolio benchmark by 30 basis points
	Volatility should not exceed 115% of the Short Duration Portfolio benchmark
Intermediate Duration Portfolio	Exceed the Intermediate Duration Portfolio benchmark by 50 basis points
	Volatility should not exceed 120% of the Intermediate Duration Portfolio benchmark
Extended Duration Portfolio	Exceed the Extended Duration Portfolio benchmark by 50 basis points
	Volatility should not exceed 125% of the Extended Duration Portfolio benchmark

REPORTING REQUIREMENTS

Treasury Responsibilities

The State Treasurer is charged with the responsibility of reporting to the Treasury Board on a monthly basis. These reports will include investment performance information, security holdings by manager, and security market values by manager. The State Treasurer has contracted with the Master Custodian to run compliance reports on the external investment portfolios. These compliance reports are comprised of various screens or tests of both individual security and total portfolio guidelines. Any significant or continuing problems will be reported to Treasury Board. Additional information will be provided if deemed appropriate or if requested. Treasury will arrange for the Master Custodian to present an annual performance review of the external investment portfolios. This Statement of Investment Policy & Goals shall be reviewed at least annually by the Treasury Staff and, if appropriate, amended at such times as the Treasury Board shall determine.

Investment Manager Responsibilities

Each investment manager shall have the responsibility to:

1. Within 30 days of each month end, reconcile all transactions, market values, security holdings, and cash flows with the General Account Master Custodian and provide a written report to the Custodian, with a copy to the Treasury of all areas of discrepancy or disagreement with the Master Custodian.

2. Report monthly performance against the benchmarks established for the account by the fifth business day of the following month. Provide quarterly written or electronic reports concerning investment strategy and economic and investment outlook by the end of the following month.

3. Provide a quarterly accounting of any professional staff turnover that would impact this relationship. Any material event that has an impact on the ownership of the investment organization or the management of this account must be reported immediately to Treasury Investment Staff.

4. Attend an annual meeting of all external portfolio managers and the Treasury Staff to review the current economic and market conditions, economic and market outlook, and the investment policies and goals of the Commonwealth of Virginia General Account Investment Fund.